UNITED STATES DISTRICT COURT
SOUTHERN DISTRICT OF NEW YORK

FIDELITY BROKERAGE SERVICES LLC and NATIONAL FINANCIAL SERVICES LLC, Plaintiffs, vs. THE FINANCIAL INDUSTRY REGULATORY AUTHORITY ("FINRA"), PETER E. DEUTSCH and WILLIAM J. DEUTSCH, Defendants.	Civ No. 15-CV-2210 (GHW) **AFFIDAVIT OF PETER E. DEUTSCH**

STATE OF NEW YORK)
) ss.:
COUNTY OF WESTCHESTER)

Peter Deutsch, being duly sworn, deposes and says:

1. I am a named Defendant in the above-captioned action. I submit this affidavit in opposition to Plaintiffs' Order to Show Cause Directing an Expedited Haring and *In Camera* Review of Materials Withheld Under the Bank Secrecy Act, 31 U.S.C. § 5318(g) and Motion to Seal. I have knowledge of the facts herein.

2. The instant proceeding devolves from a FINRA Arbitration that I commenced with my father, William J. Deutsch, which is captioned *Peter E. Deutsch and William J. Deutsch v. Fidelity Brokerage Services LLC and National Financial Services LLC* (respondents are collectively referred to as "Fidelity"), FINRA Dispute Resolution Case No. 12-02759.

3. I understand that the parties to that arbitration are before this Court because Fidelity seeks to withhold evidence of its own violations of law; and, it seeks to do so despite a ruling by the arbitral panel (after hearing substantial evidence of Fidelity's foul play) that certain documents must be produced.

4. I also understand that, by this application, Fidelity seeks to resist the production of relevant evidence of its own wrongdoing based upon a privilege associated with the reporting of misdeeds by others; *i.e.*, trying to conflate what may be baseless allegations regarding my conduct with proof of Fidelity's own unlawful conduct.

5. Given this obfuscatory tactic, I have set forth below a brief summary of a portion of the proof of Fidelity's misconduct that has surfaced. I do so not only to show that the proof sought is relevant to Fidelity's conduct (as the arbitral panel has ruled) but also to provide the Court some context; *i.e.*, in the event it does proceed with an *In Camera* review of the withheld evidence.

A. The Deutsches Join Fidelity's Family Office; The China Gold Strategy

6. My father and I began purchasing CMED shares in or about June of 2011. The investment in this Chinese health care technology company was part of a larger investment strategy (called "China Gold") devised by our investment advisor, AER Advisors ("AER").

7. The strategy was premised upon the selection of certain Chinese equity securities that were trading at extraordinarily low prices (well below real value) and the expectation that such anomalous pricing would ultimately trigger a management buy-out or another privately driven exit transaction (*e.g.*, a strategic acquisition). Market experience (as reflected by accumulated data) has demonstrated the efficacy of the China Gold strategy.

8. On November 16, 2011, I joined Fidelity's Family Office. I did so based upon multiple representations regarding the particularized service and attention provided to Fidelity's Family Office clients. For instance, Fidelity promised to provide "objective insightful investment services" delivered through a team of Family Office professionals "tasked with seamless and flawless strategy execution." A copy of FID-DEUTSCH_012902-04 is annexed hereto as Exhibit 1.

9. I also joined Fidelity because Fidelity's moniker is integrity, trust, and confidence of its customers. Specifically, Fidelity's Family Office website states "we are a cost-effective alternative for clients who want institutional capabilities delivered with objective guidance, exceptional service, integrity, and security." Fidelity and its Family Office purport to pride itself on its client experience and the "exceptional client service" that is given to every client. A copy of the webpage is annexed hereto as Exhibit 2. (See FID-DEUTSCH_012887). As part of "exceptional client service" model, Fidelity also promises to "help clients execute on their investment strategies by providing guidance, ideas, and best practices." Exhibit 3 at FID-DEUTSCH_012887. Fidelity even promises "seamless and flawless strategy execution" on behalf of their Family Office clients and "pride[s] [itself] on offering a conflict-free client service model in which [they] put [their] clients' interests first." *See* Exhibit 1 at FID-DEUTSCH_012903-04.

B. CMED Becomes Non-Margin Eligible – Fidelity Offers Its "Fully Paid Lending Program

10. On February 28, 2012, CMED was delisted by the NASDAQ. By that time, my father and I had acquired approximately 4,378,177 ADS shares of CMED. These shares, acquired before delisting, are not the prime focus of Fidelity's unlawful lending practices[1] that are a component of the claim in the Arbitration. Rather, the Arbitration focus particularly upon shares of CMED acquired after CMED resumed trading on the OTC market. My father and I actively participated (as buyers) in that market. From March 1, 2012 through June 30, 2012, we acquired an additional 8,612,843 shares of CMED.[2]

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1 These shares were transferred to accounts maintained by Deutsches investment advisor. Because the Deutsches maintained several accounts with Fidelity, they periodically conducted ordinary transfers from one account to another for the Deutsches convenience and reporting purposes.

2 The balance was acquired by William Deutsch. By June 30, 2012, the Deutsches owned almost 13 million shares of CMED.

11. Less than one week after the delisting, on March 5, 2012, Fidelity advised our investment advisor AER:

> In the managed account and a directed account with Peter Deutch [sic], there is a lending opportunity for the position in CMEDY. China Medical ADR. Our securities lending desk in Capital Markets is paying a 5% rate now currently for these hard to borrow shares. I attached a brochure that outlines the program.
>
> Please review and feel free to follow up with any questions. A MSLA, service agreement does need to be signed by the end client to enter into this program, but essentially, since there is a 100% requirement to hold this position in the account, this is money you could take in. Due to the 100% requirement the shares on loan would not effect [sic] your surplus or margin release in the account. Also there are no limitations on selling the shares.
>
> So for example, currently say you were able to lend out $1mm shares, be around $6K in the account monthly.
>
> Exhibit 4 at FID-DEUTSCH_16725 (emphasis added).

12. I have since learned that the 100% requirement referred to in the above communications is due to CMED becoming a security that is not margin eligible. Once it was delisted, Fidelity was legally barred from advancing funds respecting the CMED securities on margin; *i.e.*, unless I accepted Fidelity's offer to join its Fully Paid Lending program and signed a so-called MSLA Agreement.

13. In any case, I did not want my shares loaned; I did not want to bolster or support a short market. Accordingly, Fidelity's offer (to pay 5%) in return for the authority to loan CMED shares was rejected. And, AER advised Fidelity:

> "Client is not interested in lending stock. Thx."

Exhibit 5 AER002279.

C. Fidelity's Hypothecation of Non-Margin Eligible Shares In Contravention Of Defendants Deutsch' Direction: Not Interested In Lending Stock

14. Remarkably, Fidelity did nothing to implement my direction (not interested in lending the stock). Nor, did it ever communicate with me concerning that direction. Instead, we

have learned that Fidelity continued to lend large quantities of CMED shares (sometimes referred to as hypothecating) that accumulated in my margin accounts (all those shares were acquired after March 1, 2012).

15. Annexed hereto as Exhibit 6 is an internal memorandum reflecting that Fidelity's hypothecation was material – particularly in the illiquid market for CMED shares according to Fidelity's internal analysis:

> Fidelity had a significant loan book of roughly 1.6 mm [CMED] shares (4.9% of shares outstanding and 30% of the short interest).

Ex. 6 at FID_DEUTSCH_16628.

16. Fidelity unquestionably reaped a significant return for making these loans. But neither my father nor I was informed that our shares of CMED had been hypothecated; we were not paid any compensation for use of our shares; nor was any collateral provided to us. We never received a trade confirmation reflecting this transaction; nor was Fidelity's appropriation of their shares reflected in our account statement or portfolio review. Yet, Fidelity was obligated to do all these things if I had authorized Fidelity to hypothecate my shares; *i.e.*, consented to the Fully Paid Lending Program offered by Fidelity's March 5 email.

17. In sharp contrast to the transparency required under the Fully Paid Lending Program (described in the brochure attached to the March 5 email), I have learned through my participation in the Arbitration that Fidelity's loan desk insisted upon a "cone of silence" – that our Family Office representatives not be appraised of this "lending;" *i.e.*, so we would not learn that – despite their contrary instruction – our CMED shares had been hypothecated. Testimonial proof and documents showing Fidelity's active concealment are more fully referenced below.

D. Fidelity's Conduct Causes A Market Disruption And Short Squeeze

18. Fidelity's internal documents and the testimony adduced during the arbitration also revealed that Fidelity's covert lending boomeranged on June 11, 2012 – the day Fidelity refers t*o as the* "Deficit Determination Day." On that day, following a routine transfer of CMED shares between my margin accounts, Fidelity's hypothecation of my CMED shares triggered what its witnesses recognized as a significant "market disruption." The sequence of this market disruption is reflected in a chart prepared by Fidelity (Exhibit 7):

19. The events surrounding Fidelity's market disruption (reflected by testimony proffered by Fidelity's witnesses and also a portion of Exhibit 7 set forth below) are as follows:

- **June 11, 2012: Deficit Determination Day –** I transferred shares from my personal margin account to my AER margin account (having a lower margin debit balance).
- **June 13, 2012:** Fidelity initiates recalls of approximately 1.5 million CMED shares,[3] recalls continue over the next few days (ultimately Fidelity issues recall notices for about 1.8 million loans by June 18, 2012).[4]
- **June 15, 2012:** Ugyen Sass (the Senior Vice President and head of the Securities Lending Desk of Fidelity Capital Markets)[5] anticipates a market disruption (a short squeeze) due to Fidelity's hypothecation of CMED shares and elevates the matter for Fidelity's compliance groups to review.
- **June 19, 2012**: The recalls of approximately 1.2 million shares failed (as predicted by Mr. Sass), and Fidelity begins to buy those shares on the open

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3 Once a firm determines that it cannot support the shares that are out on loan with the shares in the customer's account –*i.e.*, the deficit determination date – a firm is required to (within a time period proscribed by regulation) issue a sufficient number of recalls of any the shares out on external loan to cure the existing deficit. Losier, Exhibit 8 at p. 107-108.

4 Recall notices for 25 loans were issued on June 13, 2012 (amounting to 1,516,700 shares). An additional 9 loans were added to the recall notices over the next several days – *i.e.*, 1 loan (55,300 shares) on June 14; 5 loans (160,800 shares) on June 15; and 3 loans (51,200 shares) on June 18. The total amount of shares recalled was 1,784,000 shares. Copies of Fidelity's Open Recalls reports during the relevant time period are annexed hereto as Exhibit 9, FID-DEUTSCH_013423-47.

5 A copy of Mr. Sass' testimony discussing the market disruption is annexed hereto as Exhibit 10 at p. 119-121.

market (a so-called "buy-in").[6]

- **June 19 -27, 2012**: Fidelity buys in approximately 1.2 million shares of CMED. (*See* Exhibit 6 at FID-DEUTSCH_16628) As a result, the price spiked (from $4 a share on June 13, 2012, to $11.80 a share on June 29, 2012).[7]

- **July 29, 2012:** Trading of CMED was halted by the SEC.

Deutsch Account Activity And Fidelity Loan Recall Status														
	6/8/2012	6/11/2012	6/12/2012	6/13/2012	6/14/2012	6/15/2012	6/18/2012	6/19/2012	6/20/2012	6/21/2012	6/22/2012	6/25/2012	6/26/2012	6/27/2012
Peter Ind. CMED Held (-790)	1,684,932	0	120,000	155,000	210,000	310,000	530,000	655,000	725,000	795,000	1,160,000	1,210,000	1,275,000	1,355,000
Peter AEP. CMED Held (-839)	4,630,000	4,680,000	4,680,000	4,682,020	4,682,020	4,682,020	4,682,020	4,682,020	4,682,020	4,682,020	4,682,020	4,682,020	4,682,020	4,682,020
Peter AEP. CMED Held (-847)	2,118,000	3,384,932	3,908,932	4,009,932	4,027,432	4,037,500	4,037,500	4,037,500	4,131,500	4,153,500	4,168,500	4,168,500	4,168,500	4,168,500
William AEP. CMED Held (-061)	2,246,000	2,246,000	2,246,000	2,246,000	2,246,000	2,246,000	2,246,000	2,311,000	2,311,000	2,311,000	2,311,000	2,311,000	2,311,000	2,311,000
William AEP. CMED Held (-525)	445,000	445,000	445,000	447,000	450,000	450,000	450,000	450,000	450,000	450,000	450,000	450,000	450,000	450,000
CMED Available to Lend	2,273,750	626,278	716,335	633,379	619,735	761,921	0	125,000	190,340	92,207	76,082	0	0	0
CMED Out on Loan to Street	1,857,900	1,876,700	1,857,900	1,739,100	1,728,600	1,450,300	1,421,300	1,144,771	960,571	846,954	675,654	599,054	589,182	
CMED Open Stock Loan Recalls (Original Contract(s) Value)				1,516,700	1,562,000	1,532,500	1,580,700	1,340,007	1,273,200	1,273,200	1,253,200	1,253,200	1,253,200	0
CMED Returned				63,800	60,500	248,300	59,000	146,529	66,800	13,617	8,600	0	0	0
Net New Recalls Issued				1,516,700	55,300	160,300	51,200	0	0	0	0	0	0	0
Remaining Recall Quantity				1,452,900	1,447,700	1,429,100	1,421,300	1,144,771	960,571	846,954	675,654	599,054	589,182	0
CMED Buy Ins	0	0	0	0	0	0	0	130,000	117,400	100,000	162,700	76,600	9372	589,182

20. Remarkably, Fidelity did not consider the foregoing market disruption (due to its substantial recalls and buy-ins of 1.2 million shares), to be troublesome; rather, Fidelity characterizes the irrational trading and price spike as being the consequences of a "normal process," a routine Fidelity practice. As Fidelity's Senior Vice President and head of Credit for Fidelity Institutional, Roger Curylo, testified:

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6 If recalls fail, Fidelity is required to buy in the securities on the open market (as "buy in"). Exhibit 8 at p. 110-111.

7 Moreover, on June 27, 2012 – the day Fidelity bought in 589,182 shares – the price of CMED increased approximately $4.

> Normal movements from different accounts into another affiliated account, let's assume with like identities, social security numbers, from Peter Deutsch to Peter Deutsch.
>
> The normal transfer [between accounts] just creates the issue of, potentially, having less shares to be lent out, because the calculation of the new account receiving it would have to go through another recalc, according to the regulations.
>
> That doesn't create, theoretically a – could create a buy-in in the Street; thus, creating, a dislocation, but it's not an intentional act. It's just normal course of business.
>
> It's very different from an intentional act versus just normal business, which is what this was.

A copy of Mr. Curylo's testimony is annexed hereto as Exhibit 11 (p. 19:2-20 emphasis added).

21. Despite this normality claim, the arbitral proceeding has focused upon Fidelity's violations of law and/or regulatory guidance, including (but not limited to):

- Securities (like CMED) that are not margin eligible and house in a margin account fall within the definition of "Fully Paid Securities" and may not be hypothecated.
- According to the NYSE, securities such as CMED that are not margin eligible (*i.e.*, subject to the 100% requirement) should have been acquired in a cash account; *i.e.*, not in a margin account. Had Fidelity complied (*i.e.*, rather than accumulating an inventory of CMED shares in margin accounts), the securities my father and I acquired after delisting would have likewise been "Fully Paid" and not legally available for hypothecation.
- Fidelity was not authorized to hypothecate securities that were not margin eligible (see below).

E. Fidelity's Arrogates Unto Itself the Authority To Hypothecate Non-Margin Securities

22. Below is an example of testimony (adduced shortly before the Panel's ruling regarding the disclosure of withheld documents) concerning the hypothecation authority granted to Fidelity under its margin agreement (*i.e.*, to hypothecate securities "you may be carrying for me on margin") and the authority which FINRA allows. (See Exhibit 12 at FID-

DEUTSCH_000979). Mr. Curylo – confronted with Fidelity's own margin agreement (upon which it relied) and FINRA's response to Fidelity's letter regarding such authority – offered the following:

Q. Is it Fidelity's practice to carry non-margin eligible securities on margin?

A. Yes.

Q. You carry non-margin eligible securities on margin?

A. All the time.

. . . .

Q. Is it your testimony that this authority that is granted to Fidelity to hypothecate securities applies to non-margin eligible securities?

A. I believe we have the right to lend out securities in that margin account.

Q. Even if they are not margin eligible?

A. Yes.

Q. You carry non-margin eligible securities on margin?

A. Yes.

Q. This is the authority you get to lend to others, right?

A. Hypothecate.

. . . .

Q. Turn to B, 19B [(Fidelity's letter to FINRA)]-- or we can turn to FINRA's response to Fidelity, but let's stay with 19B. Maybe people can read this language differently, but you need consent, signed by a customer, as written authorization to permit the loaning, that would be hypothecating, of a customer's margin eligible securities, do you see? And you just told me that that consent applies to non-margin eligible securities --

A. Those securities sit in a margin account.

Q. But that's not margin eligible as you described it to me --

A. We have lots of securities that sit in margin accounts that we do not lend money if they are in a margin account.

Q. I understand. You told me what margin eligible means, correct? CMED is not margin eligible.

A. For a loan against it.

Q. It becomes margin eligible if it is going to be hypothecated?

A. No, we reserve the right to hypothecate.

Ex. 11 at p 46: 9- 49:17. (emphasis added). But (as we have shown in the arbitration) the right that Fidelity "reserves" for itself not only exceeds the authority granted by me to hypothecate shares (only those carried on margin) but also exceeds that authority which was permitted by FINRA (*i.e.*, limited to margin eligible securities).

F. Fidelity Continued To Manifest A Callous Disregard For Me And My Father

23. Meanwhile, as Fidelity continued to profit from trading CMED shares (by both acquiring shares for me and my father, and secretly hypothecating those same shares), me and my father were aggressively purchasing CMED shares.

24. There is no question that Fidelity was well informed about this aggressive acquisition strategy. Fidelity's internal emails observed that I was bullish on CMED with an eye toward a private transaction. And as vividly reflected by a May 3rd conversation (recorded by Fidelity), Fidelity encouraged me to purchase CMED shares – trying to facilitate major block purchases.

25. Yet, Fidelity was blind to the fact that its profitable hypothecation business had become misaligned with my interests as its client. Not only did it fail to follow my instructions (or even communicate with me or my father about our interests), Fidelity failed to consider that the market disruption created by its "normal" practices was inimical to my interest: spiking the price at the same time I was aggressively purchasing shares; and, creating a market disruption

that destroyed the possibility of a potential or private exit transaction (the objective of mine and my father's investment strategy).[8]

G. Fidelity's Active Concealment

26. As noted above, Fidelity actively concealed its conduct. Fidelity's lending desk's imposition of a "cone of silence" is illustrated by the following email:

> We didn't speak directly to FFOS [(Family Office)] during buyins. Deutsche/AER[sic] were active in the name while we were buying in so didn't want to broadcast buyin impact.

Exhibit 13 at FID-DEUTSCH_14511.

27. Mr. Losier, Fidelity's Vice President of the Securities Finance Desk within Fidelity Capital Markets, also testified:[9]

> We didn't tell anyone. The only people that – you know, our treatment of buy-ins is very sensitive; and the only people that are party to the specifics of a mandatory buy-in are going to be the stock loan buy-in group that controls the process. We are going to know, as the people managing the loan book or, you know, processing the loans. And ultimately, Risk would know that there was going to be – you know, if there is a large buy-in. And then the equity trader that is going to be purchasing the shares. No other Fidelity employee and certainly no customers would be – would

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8 David Richardson (one of the key players in Fidelity's investigation) opined that the market disruption undermined a private exit strategy. *See* Ex. 6. But, Mr. Curylo (the ultimate decision maker), continued to deny that Fidelity's interests conflicted with my interests following June 11th (Deficit Determination Day):

Q. Did anybody at Fidelity suggest to you or other -- that you know of, that your interests were no longer aligned after the 11th?

A. I don't view it the way you view it. I don't view that those transactions misaligned our intentions with our client.

. . . .

Q. Do you recognize that a price spike would impact a going private strategy?

A. It's a very vague question. I can't answer it the way you are posing it.

MR. BIEDERMAN: You have to pay more for the shares.

A. Theoretically, yes.

Q. But no one in Fidelity expressed any concern that this market disruption had impacted the client's strategy?

A. Not that I know of.

Ex. 11 at p. 24:8-14; 29: 11-21.

9 Mr. Losier is responsible for leading Fidelity's securities lending activity with external broker dealers and Fidelity's fully paid lending product. He is supervised by Ugyen Sass.

have access to that information. We would consider that – very much consider that material not public information.

Q. So that information would be hidden from everybody outside of your group?

A. Yeah, we would not voluntarily – we would not share that information

Exhibit 8 (p. 29:6-24 emphasis added).

H. Fidelity Conveys False And Misleading Information

28. Not only did Fidelity impose a "cone of silence" and deliberately hide their conflicting interest from me and my father, but the information that was ultimately conveyed by Fidelity (responding to questions posed by me) was false and misleading. In multiple calls on June 18th and 19th, Amanda Topping,[10] a Family Office representative, conveyed the following false and misleading information to me:

- The recalls could not exceed 650,000 shares (and would likely be fewer shares); and
- Fidelity had 7 business days to receive the recalls (*e.g.* until June 26, 2012) and after that, if the recalls failed, buyins would commence (*e.g.*, on June 27, 2012).

See e.g., Ex. 14 at FID-DEUTSCH_009195.

29. But Ms. Topping failed to disclose that in truth:

- By June 18, 1.5 million shares were subject to recall – far more than what I was told;
- The recall process commenced days earlier – on June 13; and
- A substantial number of recalls had failed and, as a result, buy-ins (amounting to 1.2 million shares) would commence on June 19th – the same day of one of Ms. Topping's calls with me (*i.e.*, Ms. Topping falsely advised that the market disruption would not transpire – if at all – until seven days later).

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[10] Amanda Topping is a senior investment analyst with Fidelity's Family Office. She is part of a three-person relationship management team that was responsible for handling the Deutsch Family Office accounts.

I. Fidelity Investigates

30. Having imposed a "cone of silence" over its "normal process" and the resulting market disruption, Fidelity commenced an investigation into the trading of CMED. Below are several of the steps taken by Fidelity—that I have learned of through the Arbitration—to what one Fidelity witness described as a "chaotic" process:

- **June 22, 2012**: The senior vice president of Fidelity's collateral risk department, David Richardson, "escalates" the CMED trading activity to the Compliance/Surveillance teams within Fidelity. In so doing, David Richardson reports:

  > "Fidelity had a significant loan book of roughly 1.6 mm [CMED] shares (4.9% of shares outstanding and 30% of the short interest)." He further recognizes Fidelity's role in the market manipulation: "[o]bviously, the 1.2mm shares bought in by Fidelity contributed to the short squeeze (Stock Price + 7.78 pts or 185%). We still may be deficit roughly 300k with potential future 204 T+3 exposure (customer long sales)." And also opines that the short squeeze negatively impacted the Defendants Deutsch' private exit (*i.e.*, negatively impacted the client's strategy). Ex. 8 at FID-DEUTSCH_16628

- **June 27, 2012:** A conference call takes place among Fidelity's Risk, Compliance/Surveillance teams and Family office to discuss the Defendants Deutsch' trading in CMED and their motivations. Internal emails summarizing that call indicate:

  - "The reprefsentation from FFOS on our Wed conference call about this said the clients trading in CMEDY was previously reviewed by Legal and senior management in FFOS. She indicated that they felt confident the client was bullish on these companies and was buying shares with the goal of taking them private." Ex. 15 at FID-DEUTSCH_16453.

  - "The rumor is that [Mr. Deutsch] and some of his associates are buying up all the available shares with the intention of taking the company private." Ex. 16 at FID-DEUTSCH_16419.

- **June 28, 2012:** A comprehensive second level TRAP[11] report is circulated which

[11] As reflected by the testimony of both Christopher Janes and Roger Curylo, TRAP, which stands for Transaction Research Analysis Program, is part of Fidelity's monitoring and surveillance system. TRAP is a three level system that captures and analyzes data and is used to detect and report potential instances of suspicious activity.

describes the market perception that me and my father were acquiring shares with the intent of taking the company private. The report, prepared by Christopher Janes[12], after noting that I had "not placed a single sale in China Medical Technologies since [I] began acquiring the stock in late December 2011," concluded that "there appears to be a legitimate reason for the clients trading." *Id.* at FID_DEUTSCH_16422.

- In addition to the TRAP review, Fidelity's Compliance Unit undertook a further investigation. The established protocol for the investigation was described by Roger Curylo:

    - A draft report was to be completed by Compliance;
    - The draft was to be circulated to Consumer Protection (AKA Risk) for review and comment;
    - The final report is to be provided to the Family Office.

- **June 29, 2012:** All those involved in the investigation (including consumer protection and compliance) conclude that it is "incumbent" on Fidelity to speak to the client (*i.e.*, me). Ex. 17 at FID-DEUTSCH_14279; Ex. 18 at FID-DEUTSCH_16455.

- **June 29, 2012:** As Fidelity predicted, the SEC halted trading of CMED. Ex. 19 at FID-DEUTSCH_16633.

- **July 9, 2012**: The author of the TRAP report – finding that me and my father had legitimate reasons for acquiring CMED shares – noted his belief that CMED was a valuable company. He also suggested what I would say – when asked:

> "Whats [*sic*] somewhat unusual here is that China Medical Technologies appears to actually have real assets (cash on hand, real-estate [*sic*], etc) that could be sold off. It's possible that the Deutsch's [*sic*] will come back and say: "We don't care about the short sellers and negative press. China Medical Technologies has $30 million in cash-on-hand and assets that are conservatively valued at an additional $50 million. Based on our valuation, the stock is worth anywhere from $20 to $28 dollars a share." Ex. 20 at FID-DEUTSCH_16323.

- **July 10, 2012:** Representatives of Compliance and Risk speak with AER. It is also confirmed – again – that it was incumbent to speak to the client. As David Richardson testified:

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12 Christopher Janes is the Senior Risk Manager at Fidelity Investments. As a certified anti money-laundering, fraud and financial crimes investigator, through his position Mr. Janes is responsible for conducting investigative analysis based on the surveillance systems Fidelity has in place.

Q. But you understood it was incumbent upon you, Fidelity, to have that call with the Defendants Deutsch? That was what David Whitlock said?

A. Yeah.

Q. And you all Agreed?

A. We all agreed, yes.

Ex. 21 at p. 63:21- 64:1.

J. The Decision To Block Deutsches' Purchases Of CMED

31. On or about July 16, 2012, Roger Curylo, decided to block purchases of CMED by me and my father. According to Mr. Curylo, the process by which the decision was made is as follows:

- Mr. Curylo willfully ignored the TRAP report, which hypothesized that me and my father were pursuing a private transaction and concluded that "there appears to be a legitimate reason for the clients trading. That second level review was "closed out" (not elevated).[13]
- He willfully ignored the work being done by Compliance: delivery of a draft report being prepared for review by his unit was expected in early July. Ex.11 at p. 78-81.
- He willfully ignored the reports and views of those who had been involved in the investigation:
    - the trading was legitimate (and part of mine and my father's investment strategy), *id.* at p. 77, 86-87;
    - we were bullish on the Company, *id.* at p. 86-88;
    - we were pursuing a private transaction, *id.* at p. 81-82, 112-113; and
    - it was incumbent to speak to me or my father as the client, *id.* at p. 70; and
- He was aware that a price spike (or "short squeeze") occurred in late June, but he willfully ignored that the price spike was a result of Fidelity's covert hypothecation scheme (or what he referred as to part of Fidelity's "normal

[13] According to Mr. Curylo, he never received the report. Ex. 11 at p. 76-81. However, the author of the TRAP report, Mr. Janes works under Mr. Curylo's supervision and testified that he delivered the TRAP report to Mr. Curylo. *See* Ex. 22 at p. 157-60.

process"). Instead:

- While eavesdropping on the July 10th call with AER he believed the price spike was caused by me and my father paying off our margin debit balance, Ex. 11 at p. 89;
- He later (at some unspecified time) learned this was a mistake – but claims he never learned the price spike was caused by Fidelity's "normal processes," *id.*;

- He mistakenly believed that the lending desk was speaking with me and my father during the buy-in process (although he later admitted that this was another mistake). *Id.* at p. 30-32; 89
- He did not know that a series of conversations occurred between me and Amanda Topping (from Family Office) during which I was provided false and misleading information concerning the number of shares recalled and the recall and buy-in process. *Id.* at p. 30-32

32. In essence, Mr. Curylo conceded during his testimony that he bypassed and/or ignored Fidelity's established investigative process. He ignored the TRAP report prepared by Mr. Janes (who worked under his supervision). He ignored Fidelity's compliance unit and the joint investigation it had undertaken (with his own Risk unit). Mr. Curylo ignored – or dismissed as untrustworthy – the opinions of those who he testified were reliable, effective members of his own unit – as well as Compliance.

33. Mr. Curylo also purports not to have known (or considered), Fidelity's custodial problem. Yet, he had received Mr. Richardson's memorandum which advised: "We still may be deficit roughly 300k with potential future 204 T+3 exposure (customer long sales)." Ex. 6 at FID- DEUTSCH_16628. And, on July 16, 2012 it was short 400,000 shares of CMED on its own internal books. Nevertheless, while being apprised of mine and my father's—Fidelity's clients—strategy (being bullish and playing for a private exit transaction), Mr. Curylo determined to block our trading; and he did so without even considering the uniform opinion of everyone that touched this matter: it was "incumbent" to speak with the client.

34. When asked to delineate reasons for his precipitous actions, Mr. Curylo recited a number of events –mostly long past – such as the delisting of the stock, bond defaults, and auditor resignations. Yet, even Mr. Curylo could not explain why (as these same events transpired), Fidelity continued to trade significant quantities of CMED *i.e.*, purchase millions of shares of CMED – all in mine and my father's margin accounts – and profit from the secret hypothecation of those shares, amassing a loan book so large that it represented 30% of the short market.

35. Eventually, at the conclusion of his testimony, Mr. Curylo proffered the following additional explanation for his actions:

> Q. And, actually, you made the decision without consulting with Mr. Whitlock or Mr. Richardson?
>
> A. I make decisions, because that is my role. My seniority.

Ex. 11 at p. 148:18-22.

36. But, despite his seniority role, Fidelity's review and termination process was, as Amanda Topping candidly admitted, "chaotic" and "very disorganized." Thus, on the "execution date" (July 16, 2012), David Richardson advised Roger Curylo:

> Heard from FFOS on CMEDY. Saying no talking points, no communication – restriction w/o notifying client, etc. Deutsche [sic] trying to buy more shares and nobody there seems to know what to tell himb& [sic].
>
> Sounds off track b/c you guys were on calls and sending out emails post market on Friday.

Ex. 23 at FID-DEUTSCH_14660. The chaotic termination decision led one David Whitlock[14], to express his exasperation with Fidelity's conduct:

> He [Peter Deutsch] was deemed to be a 'control person', but I was not aware they blocked him from buying. It won't surprise me if this ends up a nice big legal mess involving them, his advisor, the company, the SEC, and the firm for the next few years.

Ex. 24 at FID-DEUTSCH_16572 (emphasis added).

K. Fidelity Extends Its Cone Of Silence Through The Improper Use Of Bank Secrecy Act Law

37. During the course of arbitral proceedings, Fidelity asserted a privilege objection based on the Bank Secrecy Act. The privilege objection was made after Mr. Janes was asked whether Fidelity's CMED investigation was escalated to Fidelity's evaluation and response team (a part of Fidelity's corporate security department). Fidelity articulated its objection as follows:

> MR. AMERY: I will just read this to you, "The question calls for the disclosure of confidential, non-public, supervisory information that cannot be released under Federal Regulation 12 [sic] CFR Section 103.19, that section makes the bank secrecy provisions related to certain filings applicable to broker/dealers, and under applicable Federal law the firm cannot, under any circumstances, including the context of civil litigation, disclose any such filing or confirm or deny whether any such filing exists."
>
> MR. GRAFF, SR.: So we can never know what happened?
>
> MR. AMERY: Correct.
>
> MR. BIEDERMAN: But we do know it did go further, you had subsequent phone calls, other departments were involved?
>
> MR. GRAFF, SR.: Not this department. They wouldn't tell us.
>
> MR. ANDERSON: My question is whether it went further internally or whether it went further externally, to any other governmental agency? Is there a distinction between those two or no distinction?

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[14] David Whitlock, a key player in Fidelity's investigation of CMED trading, is the Director of Compliance at Fidelity Institutional that worked in the surveillance group, which is the group that examines whether there is activity that violates Fidelity or industry rules and regulations.

> MR. AMERY: No, there is not a distinction. As I understand the requirements of the Bank Secrecy Act, we are not allowed to respond to those questions and quite frankly, I believe it is a crime. It is a crime if you respond to those questions.

Ex. 22 at p. 169:4-170:12.

38. The Deutsches urged the Panel to rule that Fidelity's objection was overbroad and legally untenable. In response, the Panel issued the following ruling:

> [T]he Panel has unanimously decided to **grant** the Motion to Compel, thus giving Claimants access to non-SAR related material thought to be withheld and leave to judicial review, if Respondents choose that course, the legitimacy of their stance.

A copy of the order issued by the Panel is annexed hereto as **Exhibit 25.**

39. Notably, the Panel delayed issuing this ruling until the 19th day of the hearing – until after hearing the substantial evidence of Fidelity's misconduct.

Peter Deutsch

Sworn to before me this
30th day of March 2015.

Notary Public
LINDA J. BAUER
Notary Public, State of New York
No. 01BA5000292
Qualified in Westchester County
Commission Expires August 10, 2018